

Washington State Auditor's Office

Audit Report

Audit Services

Report No. 58224

CITY OF WASHOUGAL

Clark County, Washington

January 1, 1994 Through December 31, 1995

Issue Date: May 2, 1997

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CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

Background

The City of Washougal has taken corrective actions and made a number of very positive commitments to improve their accounting and internal control systems following our current audit. With these improvements, the city should be on the threshold of reversing the problems which have resulted in adverse or disclaimed audit opinions on the city's financial statements for all of its audits since 1989.

Because of the complexities of financial management at the city, hiring a dedicated and competent clerk treasurer (financial manager) will also be an important and necessary component in the recovery process.

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

**Independent Auditor's Report On Compliance With Laws And Regulations
At The Financial Statement Level (Plus Additional State Compliance
Requirements Per RCW 43.09.260)**

Mayor
City of Washougal
Washougal, Washington

We have audited the financial statements, as listed in the table of contents, of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated October 18, 1996.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to the City of Washougal is the responsibility of the city's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the city's compliance with certain provisions of laws, regulations, contracts, and grants.

We also performed additional tests of compliance with state laws and regulations as required by *Revised Code of Washington* (RCW) 43.09.260. This statute requires the State Auditor to inquire as to whether the city complied with the laws and the *Constitution of the State of Washington*, its own ordinances and orders, and the requirements of the State Auditor's Office. Our responsibility is to examine, on a test basis, evidence about the city's compliance with those requirements and to make a reasonable effort to identify any instances of misfeasance, malfeasance, or nonfeasance in office on the part of any public officer or employee and to report any such instance to the management of the city and to the Attorney General. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with these provisions. Accordingly, we do not express such an opinion.

Material instances of noncompliance are (1) failures to follow requirements or violations of prohibitions contained in statutes, regulations, contracts, or grants that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or (2) considerable failure to comply with the laws and the *Constitution of the State of Washington*, the city's ordinances and orders, and the requirements of the State Auditor's Office. The results of our tests of compliance disclosed instances of noncompliance that may materially affect the financial statements, the effects of which have not been corrected in the city's financial statements. The material instances of noncompliance noted during our audit are disclosed in the accompanying Schedule of Findings.

We considered the instances of noncompliance in forming our opinion on whether the city's financial statements are fairly presented, in all material respects, in conformity with the prescribed basis of accounting and the statutory provisions described in paragraph four of this report. This report does not affect our report dated October 18, 1996, on those financial statements.

Except for the material instances of noncompliance disclosed in the Schedule of Findings accompanying this report, the results of our tests of compliance indicate that, with respect to the items tested, the city complied, in all material respects, with the provisions referred to in the third and fourth paragraphs of this report, and with respect to items not tested, nothing came to our attention that caused us to believe that the city had not complied, in all material respects, with those provisions.

This report is intended for the information of management and the mayor and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

Independent Auditor's Report On Internal Control Structure
At The Financial Statement Level

Mayor
City of Washougal
Washougal, Washington

We have audited the financial statements of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated October 18, 1996.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of the city is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with the prescribed basis of accounting. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of the city, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

The matters involving the internal control structure and its operation that we consider to be reportable conditions are included in the Schedule of Findings accompanying this report.

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we noted reportable conditions that we believe to be material weaknesses, which are identified in the Schedule of Findings accompanying this report.

This report is intended for the information of management and the mayor and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

Schedule Of Findings

1. Public Funds Were Misappropriated And Public Documents Were Falsified By The City Of Washougal Clerk/Treasurer

Our audit of the financial records of the City of Washougal revealed that at least \$977.85 in public funds were misappropriated by the clerk/treasurer, during the period March 3, 1994, to January 18, 1996. During our audit of travel reimbursements at the City of Washougal, we found the clerk/treasurer initially charged expenses on the city's VISA credit card. Subsequently, she filed claims with the Washington Municipal Treasurers Association (WMTA) and was reimbursed personally for these same expenses. Further, she claimed and received reimbursement for mileage from WMTA for a February 8, 1995, trip and, after reimbursement, submitted a false claim to the city for the same trip on February 28, 1995, for which she was also paid. A review of the accounting records found the city had not been reimbursed for these double payments. There were no federal funds involved in this case. The schedule below summarizes the city's losses by purpose of the trip and amount:

MAR 3, 1994	WMTA Board Meeting in Seattle (Air Fare/Car Rental)	\$ 87.02
FEB 8, 1995	WMTA Board Meeting in SeaTac (Mileage)	101.10
OCT 29, 1995	WMTA Conference in So. Carolina (Car Rental)	310.74
OCT 29, 1995	WMTA Conference in So. Carolina (Air Fare)	396.00
JAN 18, 1996	WMTA Board Meeting in SeaTac (Hotel)	<u>82.99</u>
Total		<u>\$977.85</u>

During an interview on December 20, 1996, the clerk/treasurer admitted she had been paid twice for the same expenses. She subsequently made restitution to the city for the full amount of these irregular transactions. RCW 42.20.060 states:

Falsely auditing and paying claims. Every public officer, or person holding or discharging the duties of any public office or place of trust under the state or in any county, town or city, a part of whose duty it is to audit, allow or pay, or take part in auditing, allowing or paying, claims or demands upon the state or such county, town or city, who shall knowingly audit, allow or pay, or, directly or indirectly consent to or in any way connive at the auditing, allowance or payment of any claim or demand against the state or such county, town or city, which is false or fraudulent or contains any charge, item or claim which is false or fraudulent, shall be guilty of a gross misdemeanor.

This misappropriation of public funds occurred because of weaknesses in the voucher system which permitted the clerk/treasurer to process claims without an adequate review by another city official.

We recommend the Washington State Office of the Attorney General and the Clark County Prosecuting Attorney review this matter and take whatever action is deemed necessary under the circumstances. Any compromise or settlement of this claim must be approved in writing by the Attorney General and State Auditor as directed by RCW 43.09.260.

Bond coverage for city employees is as follows:

Company:	Hartford Fire Insurance Company
Type Policy:	Public Employee Dishonesty
Policy No.:	PEB JI2863
Amount:	\$250,000
Period of Coverage:	March 1, 1993, until cancelled

We also recommend the city:

- a. Review its voucher system controls, correct the weaknesses outlined above, and implement an effective system of internal controls designed to ensure the protection of city assets.
- b. Notify its insurance bonding company of this loss.

Auditee's Response

The \$977.85 in question has been fully reimbursed to the City. Internal controls have been instituted which require review by the Mayor before submission by department heads for expenses for payment to the City Council. Items to be reimbursed by another agency are to be identified prior to submission of the voucher.

The City is in full concurrence that this matter should be reviewed by the Clark County Prosecuting Attorney's Office. The City will cooperate fully in that review.

2. The City Should Strengthen Controls Over Budget Preparation And Expenditures

During our review of the city's budgeting process and related expenditures, we noted internal control weaknesses and noncompliance with state laws and regulations as follows:

- a. **Budget Ordinances**) We found that the budget ordinances are not prepared in a form which makes it readily understandable what the council intended to spend during the budget year. It appears that amounts identified on the ordinance as expenditures may have included estimated ending fund balance.
- b. **Presentation in Control System**) For 1995, the budget figures in the budget control system (expenditure ledgers) do not agree with the approved budget adopted by the council for six of the 41 funds.
- c. **Presentation in Financial Statements**) In both 1994 and 1995, budget appropriations on financial statements for governmental funds do not agree with approved budget appropriations in Budget Ordinances as follows:

1994 - 18 out of 33 funds reported incorrectly
1995 - 20 out of 34 funds reported incorrectly

- d. **Budget Over Expenditures**) Eight funds were apparently overspent according to the city's financial statements during 1994 and one fund was overspent in 1995. However, we could not verify the accuracy of budget figures on these statements due to problems with the budget document (item a.) discussed earlier. Funds overspent, per the financial statements, are listed below:

<u>Year</u>	<u>Fund Number) Fund Name</u>	<u>Amount Over Spent</u>
1994	No. 101-Street Fund	\$7,794
	No. 102-Arterial Street Fund	7,005
	No. 105-Cumulative Park Fund	214
	No. 114-Social Service Center	1,168
	No. 120-ACC Fire Equipment	6,526
	No. 124-Computer Equipment Fund	3,508
	No. 206-1990 GO Bond Fund	154
	No. 604-Cemetery Perpetual Fund	45
1995	No. 206-1990 GO Bond Fund	220

Expenditures in excess of budget are contrary to the limitations contained in RCW 35A.33.120, which states in part:

. . . The expenditures as classified and itemized in the final budget shall constitute the city's appropriations for the ensuing fiscal year. Unless otherwise ordered by a court of competent jurisdiction, and subject to further limitations imposed by ordinance of the code city, the expenditure of city funds or the incurring of current liabilities on behalf of the city shall be limited to the following:

- (1) The total amount appropriated for each fund in the budget for the current fiscal year

We recommend city officials enact budget ordinances which clearly reflect expenditure limits imposed on each of its funds. Additionally, we recommend city officials establish controls to ensure budget appropriations are properly accounted for in the budget control system and are properly presented in financial statements.

Auditee's Response

Controls over Budget Preparation and Expenditures

- a. *The Finance Director will insure that future budget ordinances will reflect the budgeted Ending Fund Balance separately from the Expenditures in order to insure full understanding by the City Council and Administration as to the approved expenditure budgets.*
- b. *The Finance Director will insure that the budget preparation process is followed through each year.*
- c. *Preparation of the financial statements will be verified to the budget ordinances as approved by City Council.*
- d. *The changes for the Accounts payable process and more frequent monitoring of expenditures will increase the accuracy of posting in the future.*

- e. *Changes that are addressed in item (a) will follow through to correct these problems as well.*

3. The City Should Improve Controls Over Cash Receipting

During our review of the city's cash receipting system, we noted significant control weaknesses. Specific problem areas are discussed below.

- a. **Treasurer's Receipts**) City cashiers do not account for all voided receipts, nor do they include the mode of payment (cash or check) on all receipt forms, making it impossible to verify revenue collections to the composition of deposits. Several different cashiers use the same cash drawer as well as a variety of different manual cash receipt books. These practices make it possible for moneys to be received but not deposited and makes it difficult to fix responsibility for any potential losses or irregularities.
- b. **Utility Billing and Receipting System**) The same individual performs a variety of incompatible duties, including determination of charges due, customer billing, cash receipting, and posting of transactions to accounting records. These functions are also performed without adequate review. Additionally, noncash credits are sometimes posted to individual utility accounts without sufficient documentation to disclose why the adjustments were made. No one reviews or reconciles the adjustment ledger to approved source documents to ensure that adjustments to accounts have been properly authorized by management.
- c. **Building Permits and Plan Check Fees**) We were unable to verify whether all revenues were collected or reported from these sources because of internal control system weaknesses. Unused or voided building permits were discarded and prenumbered receipts were not used. Permits issued were never reconciled to revenues collected. These conditions make it possible for cash to be removed without being detected and also make it impossible to account for the completeness of the revenue reported.

Taken individually, these conditions are significant weaknesses. Collectively, they indicate pervasive internal control problems, which needlessly expose the city to the risk of fraud or abuse. These conditions occurred because the director of finance did not make sufficient effort to correct the control weaknesses identified in our 1992-93 audit report and permitted the internal controls to continue to deteriorate.

We recommend the city council ensure that the director of finance establish and implement internal controls over all cash receipting procedures, including instituting numeric receipting, proper segregation of employee duties, and management review of pertinent transactions.

Auditee's Response

Controls over Cash Receipting

After the audit field work was completed, we have consolidated cash receipting as a "Cashier" function only. Independent cash drawers have been established. Written procedures have been implemented.

Utility billing procedures are included in the re-organization of the Finance Department. The Utility Billing Specialist does not receive customer payments at all. Customer payments are posted by the City Accountant. The Utility billing process has been formalized. Processes include review and approval of adjustments by management prior to posting and review after posting.

Building permit and plan check changes have been implemented by the Planning Director as well. Numbered permits are used and voided permits are being maintained as part of the record.

4. The City Should Strengthen Controls Over Payments For Goods And Services

During our review of the City of Washougal's system for payment of goods and services, we noted internal control weaknesses and noncompliance with state laws and regulations as follows:

- a. **Poor Disbursement Practices)** The city issued checks out of a "Claims and Payroll" checking account. Employees did not account for the numerical integrity of the check stock, and did not present all checks to council for approval. City employees also improperly voided and reissued checks and did not record all checks in the check register.
- b. **Incompatible Duties)** The assistant clerk/treasurer issued checks from both the Treasurer's Checking Account and the Warrant Disbursement Account, and also reconciled the Treasurer's Checking Account. The utility billing clerk prepared some vouchers for payment and was also an authorized signer on both the Treasurer's Checking Account, and the Warrant Disbursement Account. These practices violate the tenants of good basic internal control. No individual should have control over both cash and the accountability for cash. We did not find sufficient compensating controls to diminish the risk presented by these weaknesses.
- c. **Inadequate Supporting Documentation)** A significant number of disbursements were made without adequate documentation to support their validity. During our review, we found instances of the following types of payments without adequate supporting documents:
 - Payments to police reservists for hours worked which had no supporting documents attached.
 - A payment to an employee for tuition reimbursement without a supporting invoice or copy of employee check as proof of payment.
 - Payments to employees for travel related reimbursements with inadequate or no invoices to support the expense and no proof of a business purpose for the trip. The persons who attended the meetings were sometimes not identified, nor was a travel expense claim form always used.
 - Payments to a vendor for an amount less than the invoice amount without any explanation.
- d. **Improper Payment Approval)** The following payments were made without appropriate approvals:
 - Payment to an employee for tuition, without the mayor's approval as specified in the collective bargaining agreement.
 - Payment to the finance director for travel reimbursement which was not properly approved.

- Payment to a vendor for solid waste collection without evidence that it had been reviewed by the utility billing clerk.
- None of the payments we reviewed contained the required auditing Officer's signature. Voucher forms contained the proper certification statement, but the Auditing Officer did not sign them. This practice violates RCW 42.24.080, which states in part:

All claims presented against any county, city . . . shall be audited, before payment, by an auditing officer elected or appointed . . . Such claims shall be prepared for audit and payment on a form and in the manner prescribed by the state auditor. The form shall provide for the authentication and certification by such auditing officer that the materials have been furnished . . . and no claim shall be paid without such authentication and certification

As a result of the violations and weaknesses cited, council has been denied the fundamental opportunity to disapprove those checks which are not presented to them for approval. Without proper documentation, officials do not have adequate information for determining the appropriateness of expenditures. In addition, the city is at risk of paying improper claims presented.

These violations and weaknesses exist primarily because city management has not put sufficient emphasis on instituting and maintaining effective internal control systems.

We recommend the city establish controls to ensure the following:

- All checks are accounted for in numerical sequence and provide for council review of all disbursements.
- Tasks are assigned to staff in a manner which avoids the performance of incompatible duties.
- All disbursements are supported by adequate documentation to allow staff to establish their validity and reasonableness.
- Travel policy be amended to include all employees, covering all forms of reimbursement, and containing language to ensure that all requests contain adequate support to establish the public purpose of the expenditure.
- All disbursements are adequately approved by the appropriate department head or other city official.
- All disbursements are approved by the auditing officer in the proper certification area of the voucher form prescribed by council.

Auditee's Response

Controls over Cash Disbursements

- a. *Numerical integrity of the check stock is included as part of the Accounts payable process.*

- b. *Reconciliations are now being done by the Finance Director. Accounting Specialist - A/P has been removed from both bank accounts as an authorized signature. The Utility Billing Specialist no longer is involved in the Accounts payable function.*
- c. & d. *Payments are being reviewed on a much more comprehensive basis. Changes in process have been implemented by using a "Claim Voucher" form and having the Auditing Officer sign the document. Written procedures have been developed to insure that the proper documentation and approval takes place.*

City Council finance Committee reviews all bills which are presented for payment. They only sign the Voucher Register form as a matter of convenience, but have access to all documentation that has been presented for payment.

5. The City Should Strengthen Controls Over Payroll Procedures

During our review of the City of Washougal's payroll system, we noted the following internal control weaknesses and violation of state law:

- a. **Inappropriate Pay Raise Authorizations)** The mayor authorized pay raises for the public works director and finance director without approval of city council. The increases were not discussed in an open public meeting nor were they adopted by ordinance as required by RCW 35A.12.020, which states:

The authority, duties and qualifications of all appointive officers shall be prescribed by charter or ordinance, consistent with the provisions of this title, and any amendments thereto, **and the compensation of appointive officers shall be prescribed by ordinance** (Emphasis ours)

When management makes these types of payroll adjustments without proper approval of the city council, the governing body does not have the opportunity to determine whether pay increases are appropriate. This situation occurred because the mayor directed staff to make these payments to employees without obtaining prior approval of city council as required by law.

- b. **Time Sheet And Leave Approval)** Time sheets were prepared by each department head but lacked final review and signature by a higher authority. The mayor approved their leave slips but he did not match the leave taken to the time sheets submitted for that period. The leave hours recorded on time sheets did not agree with the leave taken, according to leave slips, during the period July 26, 1995, to August 25, 1995, for both the public works director and the finance director. This discrepancy brings into question the accuracy of vacation time accrued for these managers, especially since the approved leave slips are not used as the source document for recording the leave taken.

Because of these weaknesses, leave balances and the city's liability could potentially be overstated. This could also allow employees to take more leave than they are entitled. The weaknesses occurred because the payroll clerk was not required by management to reconcile the leave records to the time sheets.

We recommend city council set all salaries and wages for employees including appointed department heads. We further recommend the mayor sign all time sheets for appointed

department heads before payroll is prepared and ensure approved leave slips agree with the leave hours recorded on the time sheet.

Auditee's Response

Controls over Payroll

- a. *An ordinance was presented at the February 3, 1997 council meeting to set the salaries of the Department Directors.*
- b. *Department managers are only submitting time exceptions to the mayor for review and approval.*

6. The City Should Strengthen Controls Over Cellular Phone Usage

Personal Cellular Telephones) During our review of the City of Washougal's cellular phone charges, we noted the city allows all of its employees to purchase cellular phones with their personal phone usage billed on the city contract with AT&T Wireless. The voucher clerk identifies personal phone charges, tracks payment collection from employees, and remits them to the vendor. The city has a written agreement with individual employees specifying how unpaid charges would be resolved. However, the use of staff time to identify amounts owed and collect payments for personal phone bills is an inappropriate use of city employee time.

City Owned Cellular Telephones) In addition, the Mayor, all department heads, and certain other employees have cellular phones purchased by the city, which ostensibly may be used for both business and personal purposes. The city attorney, who is in private practice, also has a cell phone provided by the city. For any personal calls made on these phones, the voucher clerk may, or may not, collect from the individuals involved and remit the employee's personal payment to the vendor in the following month's billing cycle. The clerk does not keep a record of these payments and, for the charges we reviewed, was unable to determine whether the personal charges had been reimbursed to the city. The failure to adequately track reimbursements for personal calls made on city phones is a weakness in the city's voucher system.

We recommend city officials develop and implement policies and procedures that would strengthen the controls over cellular phone use. City officials should consider the following when developing the policies and procedures:

Personal Cellular Telephones:

Ensure staff are not spending city time to identify, track, collect, and make payments for personal phone charges.

- Ensure the employees are responsible for paying the entire amount of their personal phone bill. Reimbursement for any business calls made on these personal phones should be requested through the employee expense claim process.

City Owned Cellular Telephones:

- Officials should determine who is eligible for a cellular phone and for what purposes a cellular phone is authorized. Eligibility should be based on whether the city benefits substantially from the individual having cellular phone access.

- The city should develop a system for identifying any personal use of city owned cellular phones and ensure that all personal use is reimbursed by employees in a timely manner.

Auditee's Response

Controls over Cell Phones

The cell phone policy has been reviewed. The City as requested that AT&T remove employee owned cell phones from the City's account no later than February 28, 1997. City owned cell phones are to be the only listed phones on the account.

The personnel policies which were adopted by council in July 1996 allow use of city owned cell phones for personal calls but require reimbursement of personal calls to the city. Agreements with employees who are in custody of city owned cell phones will be included in their files in order to collect for personal calls in the event that an employee doesn't follow the reimbursement procedure. The reimbursement procedure will allow for an audit trail of reimbursement to the City of personal calls.

7. The City Should Improve Accounting Controls Over Its Combined Utility Operations

During our review of the city's accounting systems, including capital assets, utility billing, and accounts receivable, we noted significant internal control weaknesses, as follows:

- a. **Water-Sewer Fixed Asset System**) We have issued adverse opinions on the city's financial statements every year since 1990, primarily due to material and pervasive misstatements in the city's water sewer utility asset balances. During the current audit, we were unable to verify the accuracy of the Property, Plant and Equipment Asset balances recorded at December 31, 1994, and 1995, on the city's utility balance sheet. For both years, we found the total amounts recorded on the balance sheet did not match the amounts recorded in the general ledger. Additionally, the general ledger did not agree with the subsidiary ledgers where the individual asset costs are recorded. Beyond this, we were unable to verify the accuracy of asset costs recorded in the subsidiary ledgers. In 1994, the city set up new subsidiary ledgers to improve their asset accounting. However, they remain unable to produce verifiable information in support of figures shown as asset costs on the new subsidiary ledgers and the asset accounting system continues to be faulty and unreliable. These discrepancies violate the basic tenants of asset accounting, including the requirement for documentation to support subsidiary asset ledgers, which accurately reflect the city's asset costs. These figures must also be traceable through the general ledger and finally be accurately recorded on the city's utility balance sheet.
- b. **Accounts Receivable System**) At December 31, 1995, accounts receivable subsidiary balances, where individual customers balances are recorded, were significantly less than the total accounts receivable shown on the balance sheet. Management was not aware of the difference and could not account for it. This is a serious breakdown of fundamental business accounting convention. Total customer accounts receivable listings must equal the total accounts receivable control.
- c. **Inappropriate Accounting Entries**) For both years audited, we noted several instances where accounting entries had been made inappropriately. All of the items listed below affected the combined utility financial statements and should have been properly recorded. These are examples of some of the erroneous entries and do not

constitute an exhaustive listing of all the erroneous accounting entries discovered during the audit.

(1) Water-Sewer 1994 net income was overstated by an inappropriate prior period adjustment of \$392,809. Prior period adjustments should be recorded to the Retained Earnings account, and not have an effect upon net income in the current period. In this case, if this entry had been properly entered, the utility would have shown a net loss instead of net income for 1994.

(2) In 1995, they inappropriately recorded a liability of \$103,302 to offset a capital lease receivable of the same amount.

(3) Construction Work in Process was not recorded for either 1994 or 1995. The utility had construction projects in both years and should have recorded costs related to these projects.

(4) Revenues for charges for services were overstated for both years because the amounts recorded did not agree with supporting subsidiaries.

(5) Sewer lines installed prior to 1994 were recorded once as \$807,422, and once as \$1,496,080. This is an apparent duplicate entry.

(6) Depreciation Expense recorded for 1994 at \$174,848 did not agree with depreciation expense recorded in the subsidiary ledger at \$209,781.

Because of the accounting system weaknesses discussed above, resulting in the uncertainty of material fixed asset balances (a), accounts receivable balances (b), and the other identified misstatements (c), which materially affect the city's utility financial statements, we are unable to express an opinion on the city's financial statements for either 1994 or 1995.

These weaknesses occurred because the city's clerk/treasurer was, in some cases, not aware of the problems present in the accounting system and, in other cases, was apparently unaware of proper accounting treatments.

We recommend the city establish controls to ensure the accounting systems are corrected and to ensure financial statements reflect information contained in the related accounting records, from which financial statements are prepared. We further recommend the city council ensure the inappropriate accounting practices that have continued to occur over the past six years are corrected and that financial statements are properly prepared in the future.

Auditee's Response

Combined Utility Operations

The issues on this were discussed with the Regional Audit Manager. To address the issues for the Fixed Asset System, the documentation for prior period adjustments and changes back to the 1989 financial reports will be included and provided within the 1996 Financial report and addressed by the auditors at the next audit. Support of asset values will be provided either through purchase documents or through documentation of current value estimates.

Reconciliation of the accounts receivable subsidiary ledgers to the General Ledger control account is part of the month end processing that is done by the Utility Billing Clerk. As part of the changes to a Category I reporting entity, we are treating utility billing as a true account receivable.

The Finance Director will be more involved in the preparation and the review process for preparing accounting entries and the statements for the utilities operations. Corrections will be made in the 1996 financial statements and the statements will be prepared properly.

8. The City Should Prepare And Submit Accurate Annual Financial Reports

The city is required to annually submit a variety of reports and supplemental schedules to the State Auditor's Office. We found significant errors in the documents listed below, during our audit:

Fund Resources and Uses Arising From Cash Transactions (C-4) 1994 and 1995
Fund Resources and Uses Arising From Cash Transactions (C-5) 1994 and 1995
Long Term Debt (Schedule 09) 1994 and 1995
Cash Activity (Schedule 11) 1994 and 1995
Financial Assistance (Schedule 16) 1994 and 1995

Additionally, the city prepared a Schedule of Warrant Activity for both years. Since the city does not issue warrants, but instead uses commercial bank checks, this activity should be reflected on the Schedule of Cash Activity. The figures on the warrants schedule appear to be the activity of their payroll and claims clearing checking account in a commercial bank. Consequently, the Schedule of Warrant Activity is not necessary and its use could cause readers to be misled. RCW 43.09.230 states in part:

The state auditor shall require from every taxing district and other political subdivisions financial reports covering the full period of each fiscal year, in accordance with the forms and methods prescribed by the state auditor, which shall be uniform for all entities of the same class . . . **The reports shall contain accurate statements**, in summarized form, of all collections made, or receipts received, by the officers from all sources; all accounts due the public treasury, but not collected; and all expenditures for every purpose, and by what authority authorized (Emphasis ours)

We also published a similar finding in our 1992-93 audit report concerning inaccuracies in some of these same reports. When the city does not prepare and file accurate financial reports, users of the reports are denied access to reliable financial information. Users and their concerns include:

- a. The city council which may use these reports as a management tool.
- b. The general public interested in reports on the cost of public services.
- c. The Washington State Legislature which receives the annual volume of comparative statistics for municipalities published pursuant to RCW 43.09.230.
- d. The Office of State Auditor's staff who note that inaccurate financial reports prolong audit work and, correspondingly, increase audit costs.

The reason the reports and schedules contain repeated, pervasive errors is that the clerk/treasurer did not accept responsibility for ensuring accuracy in the finished product.

We recommend the city council take action necessary to ensure the accurate preparation of annual reports in accordance with statutory requirements.

Auditee's Response

Accurate Financial Reports

The city is changing the method of reporting from Category II (cash basis) to Category I (full or modified accrual basis). This is a big undertaking, but it will create a consistency in reporting. The City will continue making improvements in this area. The Finance Director will insure that the financial statements are prepared accurately.

9. The City Should Strengthen Controls Over Contracts And Payments For Services

During our review of the City of Washougal's contracts and related payments for services, we noted internal control weaknesses and noncompliance with state laws and regulations as follows:

a. **Contract Approval)** We found no evidence of approved written agreements for the following services:

- District Court services provided by Clark County. The Clark County District Court Administrator indicated that the court has been unsuccessful in its attempts to get a signed contract with the City of Washougal.
- Legal services provided by the city attorney. Payments have been made for these services without a written, approved contract.

With regard to contracts requiring writings, Chapter 19.36 RCW states:

In the following cases, specified in this section, any agreement, contract and promise shall be void, unless such agreement, contract or promise . . . be in writing, and signed by the party to be charged therewith, or by some person thereunto by him lawfully authorized, that is to say: (1) Every agreement that by its terms is not to be performed in one year from the making thereof

b. **Payment Approval)** The following payments were made without adequate internal controls:

- Payments to Evergreen Waste Systems totaling \$310,569 in 1995 for solid waste collection and disposal were approved by the clerk/treasurer without evidence that they had been reviewed for accuracy by comparing them to the city utility accountant's independent calculations.
- Payments to a local firm for attorney services totaling \$41,383 were made in 1995 without a contract. In addition to specifically identified charges, the payments included \$2,000 per month in unsupported charges. The payments were apparently a monthly retainer. However, we found no contract authorizing such payments or detailing services included in the retainer.
- Payments to the City of Camas for equipment rental totaling \$9,718 during 1995 were made at varying rates without documentation to support that the

rates charged were correct and properly chargeable to the City of Washougal.

- Payments to Clark County for District Court services were made without adequate documentation to support validity of amounts paid.

As a result of the weaknesses cited, staff does not have adequate information for gauging the reasonableness of expenditures and the city is at risk of potential claims.

These weaknesses exist primarily because city management has not put sufficient emphasis on instituting and maintaining effective internal control systems.

We recommend the city establish controls to ensure payments to vendors are made in accordance with written agreements and are adequately documented to ensure their accuracy and propriety.

Auditee's Response

Controls over Contracts and Payments for services

Contracts have been approved in January for District Court and Attorney was approved in February.

Procedures for approval of garbage charges are formalized. This will include marking on the bill in order to show review by the appropriate person.

Equipment that is "rented" from City of Camas is under joint ownership. The approval of the billings by the PW Superintendent will reference the current rate resolution in force.

Auditor's Concluding Remarks

We appreciate the city's responsiveness to our audit report findings by both correcting and proposing to make the changes necessary to strengthen the accounting and internal control systems. We will review the city's progress during our next audit.

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

**Independent Auditor's Report On Financial Statements And Additional
Information**

Mayor
City of Washougal
Washougal, Washington

We were engaged to audit the accompanying financial statements of the individual funds of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, as listed in the table of contents. These financial statements are the responsibility of the city's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1 to the financial statements, the city prepares the financial statements for its proprietary funds on the basis of accounting prescribed by the State Auditor in the *Budgeting, Accounting and Reporting System* (BARS) manual. This basis conforms to generally accepted accounting principles applicable to proprietary funds of local governments.

As described in Note 1 to the financial statements, the city prepares its financial statements for the remaining funds on the basis of accounting prescribed by Washington State statutes and the *Budgeting, Accounting and Reporting System* (BARS) manual prescribed by the State Auditor. This prescribed basis of accounting is a basis of accounting other than generally accepted accounting principles.

We were unable to verify material property, plant, and equipment asset balances on the city's Water-Sewer Fund balance sheets for either 1995 or 1994, due to pervasive problems in the city's system of accounting for these assets. We were unable to substantiate accounts receivable balances for the water-sewer utility, or the refuse collection fund, since subsidiary ledgers did not agree with amounts reported on the balance sheet. We found several material, inappropriate accounting entries, including the erroneous treatment of a prior period adjustment, erroneous treatment of a capital lease, failure to record construction in progress, overstatement of revenues, double recording of assets, erroneous depreciation entries, and a number of other errors affecting the financial statements of the city's utilities. We found that the budget appropriations reported for most funds on the city's 1995 and 1994 financial statements did not agree with the budget ordinances approved by the city council.

Because of the pervasive errors, omissions, and misstatements in the city's financial statements discussed above and in our Schedule of Findings, and the uncertainty which currently exists regarding amounts which should have been recorded, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements referred to above.

Our audit was made for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Schedules of Long-Term Debt and the Schedules of State Financial Assistance are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 18, 1996, on our consideration of the city's internal control structure and a report dated October 18, 1996, on its compliance with laws and regulations.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

Independent Auditor's Report On Supplementary Information
Schedule Of Federal Financial Assistance

Mayor
City of Washougal
Washougal, Washington

We have audited the financial statements of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated October 18, 1996. These financial statements are the responsibility of the city's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Our audit was made for the purpose of forming an opinion on the financial statements of the City of Washougal taken as a whole. The accompanying Schedules of Federal Financial Assistance are presented for purposes of additional analysis and are not a required part of the financial statements. The information in the schedules has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

**Independent Auditor's Report On Compliance With The General Requirements
Applicable To Federal Financial Assistance Programs**

Mayor
City of Washougal
Washougal, Washington

We have audited the financial statements of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated October 18, 1996.

We have applied procedures to test the city's compliance with the following requirements applicable to its federal financial assistance programs, which are identified in the Schedules of Federal Financial Assistance, for the fiscal years ended December 31, 1995 and 1994:

- Political activity
- Davis-Bacon Act
- Civil rights
- Federal financial reports
- Allowable costs/cost principles
- Drug-Free Workplace Act
- Administrative requirements, including subrecipient monitoring

The following requirements were determined to be not applicable to its federal financial assistance programs:

- Cash management
- Relocation assistance and real property acquisition

Our procedures were limited to the applicable procedures described in the Office of Management and Budget's (OMB) *Compliance Supplement for Single Audits of State and Local Governments* or alternative procedures. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the city's compliance with the requirements listed in the preceding paragraph. Accordingly, we do not express such an opinion.

With respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the requirements listed in the second paragraph of this report. With respect to items not tested, nothing came to our attention that caused us to believe that the city had not complied, in all material respects, with those requirements.

This report is intended for the information of management and the mayor and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also

serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

Independent Auditor's Report On Compliance With Specific Requirements
Applicable To Nonmajor Federal Financial Assistance Program Transactions

Mayor
City of Washougal
Washougal, Washington

We have audited the financial statements of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated October 18, 1996.

In connection with our audit of the financial statements of the city and with our consideration of the city's control structure used to administer its federal financial assistance programs, as required by OMB Circular A-128, *Audits of State and Local Governments*, we selected certain transactions applicable to certain nonmajor federal financial assistance programs for the fiscal years ended December 31, 1995 and 1994. As required by OMB Circular A-128, we have performed auditing procedures to test compliance with the requirements governing allowability of the program expenditures that are applicable to those transactions. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the city's compliance with these requirements. Accordingly, we do not express such an opinion.

With respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the requirements listed in the preceding paragraph. With respect to the items not tested, nothing came to our attention that caused us to believe that the City of Washougal had not complied, in all material respects, with those requirements.

This report is intended for the information of management and the mayor and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

**Independent Auditor's Report On Internal Control Structure Used In
Administering Federal Financial Assistance Programs**

Mayor
City of Washougal
Washougal, Washington

We have audited the financial statements of the City of Washougal, Clark County, Washington, as of and for the fiscal years ended December 31, 1995 and 1994, and have issued our report thereon dated October 18, 1996.

We conducted our audit in accordance with generally accepted auditing standards, *Government Auditing Standards*, issued by the Comptroller General of the United States, and the provisions of OMB Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing our audit, we considered the city's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and to report on the internal control structure in accordance with OMB Circular A-128. This report addresses our consideration of internal control structure policies and procedures relevant to compliance with requirements applicable to federal financial assistance programs. We have addressed internal control structure policies and procedures relevant to our audit of the financial statements in a separate report dated October 18, 1996.

The management of the city is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- Assets are safeguarded against loss from unauthorized use or disposition.
- Transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with the prescribed basis of accounting.
- Federal financial assistance programs are managed in compliance with applicable laws and regulations.

Because of inherent limitations in any internal control structure, errors, irregularities, or instances of noncompliance may nevertheless occur and not be detected. Also, projection of any evaluation of the

structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures used in administering federal financial assistance programs in the following categories:

- **Accounting Controls**
 - Cash receipts
 - Cash disbursements
 - Accounts payable
 - Purchasing and receiving
 - Payroll
 - General ledger
- **General Requirements**
 - Political activity
 - Davis-Bacon Act
 - Civil rights
 - Federal financial reports
 - Allowable costs/cost principles
 - Drug-Free Workplace Act
 - Administrative requirements, including subrecipient monitoring
- **Specific Requirements**
 - Types of services
 - Reporting
- **Claims For Advances And Reimbursements**

For all of the applicable internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and determined whether they have been placed in operation, and we assessed control risk.

The following internal control structure categories were determined to be insignificant to federal financial assistance programs:

- **Accounting Controls**
 - Receivables
 - Inventory control
 - Property, plant, and equipment
- **General Requirements**
 - Cash management
 - Relocation assistance and real property acquisition
- **Specific Requirements**
 - Eligibility
 - Matching, level of effort, earmarking
 - Special requirements
- **Amounts Claimed Or Used For Matching**

During the fiscal year ended December 31, 1995, the city had no major federal financial assistance programs and expended 100 percent of its total federal financial assistance under the following nonmajor federal financial assistance program: Community Development Block Grant (CFDA 14.218).

We performed tests of controls, as required by OMB Circular A-128, to evaluate the effectiveness of the design and operation of internal control structure policies and procedures that we considered relevant to preventing or detecting material noncompliance with specific requirements, general requirements, and requirements governing claims for advances and reimbursements, and amounts claimed or used for matching that are applicable to the aforementioned nonmajor program. Our procedures were less in scope than would be necessary to render an opinion on these internal control structures policies and procedures. Accordingly, we do not express such an opinion.

Our consideration of the internal control structure policies and procedures used in administering federal financial assistance would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a reportable condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that noncompliance with laws and regulations that would be material to a federal financial assistance program may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operation that we consider to be material weaknesses, as defined above. We found a number of weaknesses in the city's internal control system, as reported in our Schedule of Findings. However, these weaknesses did not significantly impact the systems which processed the receipts and expenditures made under the federal grants during the years we audited.

This report is intended for the information of management and the mayor and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

BRIAN SONNTAG, CGFM
STATE AUDITOR

October 18, 1996

CITY OF WASHOUGAL
Clark County, Washington
January 1, 1994 Through December 31, 1995

Status Of Prior Findings

The findings contained in the prior audit report were resolved as follows:

1. The City Should Improve Controls Over Cash Receipts

Resolution: The city continued to have problems in this area during our 1994-95 audit as indicated in Finding 3. City officials have now taken steps to eliminate the problems indicated.

2. The City Should Strengthen Controls Over Contracts And Payments For Solid Waste Collection And Disposal

Resolution: The city continued to have problems in this area during our 1994-95 audit as indicated in Finding 9. City officials have now taken steps to eliminate the problems indicated.

3. The City Should Prepare And Submit Accurate Financial Reports

Resolution: The city continued to have problems in this area during our 1994-95 audit as indicated in Finding 8. City officials have now taken steps to eliminate the problems indicated.